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S E C R E T SECTION 01 OF 05 DAMASCUS 000327

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SUBJECT: PART 1: SYRIA'S CHANGING FINANCIAL LANDSCAPE -
PUBLIC BANKING

REF: A. DAMASCUS 189

[1](#)B. 08 DAMASCUS 735

[1](#)C. 08 DAMASCUS 727

[1](#)D. 08 DAMASCUS 742

[1](#)E. DAMASCUS 307

Classified By: Charge d'Affaires Maura Connelly for reasons 1.4(b,d)

Summary

[1](#)1. (C) Nearly 40 years after Syria's banking industry was nationalized, Law No. 28 of 2001 authorized the re-introduction of private banking. Eight years on, Law No. 28 has had the most visible impact of President Bashar al-Asad's many economic "reforms," and has generated significant spinoff legislation. Although Syria's expanding banking market is still dominated by six state-owned public banks, U.S. sanctions against the Commercial Bank of Syria (CBS) and internal political resistance to reform are eroding their position in an increasingly competitive industry. While the absence of publicly-available audited financial statements makes judging the public banks' performance difficult, informed contacts report that only Real Estate Bank (REB) earns a profit. Prime Minister Utri recently instructed CBS to sell its stake in REB in an attempt to help REB open an account in a U.S. bank for processing U.S. dollar transactions, presumably to improve REB's competitiveness. While market trends gradually shift toward private banking, some regime elements are driving the expansion of public banking, such as the Syrian-Iranian Commercial Bank. End Summary.

[1](#)2. (SBU) This is the first cable in a four-part series

examining Syria's financial sector. It should be read in conjunction with septel cables on moneychangers, private banks, and the Central Bank of Syria.

Banking Sector Getting Crowded

¶3. (U) Nearly 40 years after Syria's banking industry was nationalized in the Ba'athist revolution of 1963, Law No. 28 authorized the re-introduction of private banking in 2001. The most visible of President Bashar al-Asad's economic "reforms," Law No. 28 sparked an industry boom -- despite restricting foreign ownership of private Syrian banks to 49 percent. In 2003, Bank BEMO Saudi Fransi (BBSF) became the first private bank to open in Syria, followed in quick succession by Bank of Syria and Overseas (BSO) and the International Bank for Trade and Finance (IBTF). Decree 35 of 2005 established Islamic banking in Syria, and by 2009 some nine traditional private banks and three Islamic banks were in operation. By mid-2009, seven more prospective banks had applied to the Central Bank of Syria (CBoS) for licensing.

¶4. (C) Against this backdrop, six state-owned public banks continue to operate in Syria. Contacts report that Syria's public banks are structured as closed joint stock companies, with the Ministry of Finance holding majority ownership and other government entities holding minority positions. The largest of the six is the Commercial Bank of Syria (CBS), which was designated by the Treasury Department in 2004 under

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Chapter 311 of the USA Patriot Act as an institution of primary money laundering concern. CBS is reportedly a minority shareholder in four of the five other public banks -- the Agricultural Cooperative Bank (ACB), founded in 1888; Industrial Bank, founded in 1959; Popular Credit Bank, established in 1966; and Savings Bank, established in 2000. Until December 2008, CBS also held shares in Real Estate Bank (REB), founded in 1966, but Prime Ministerial Decision No. 5533 facilitated the sale of CBS's 0.2 percent shares (worth about USD 63,025) to the Syrian Public Insurance Establishment -- a maneuver designed to try to shield REB from the stigma of U.S. sanctions (see paras 10-12).

Public Banks Losing Ground, but Still Dominant

¶5. (C) According to a 2008 survey conducted by the private business intelligence and consulting firm Strategic Axis Advisors (protect), Syria's private banks have taken a significant bite out of the public banks' market share in a relatively short period of time. Since 2004, the public banks' share of total Syrian banking deposits decreased from 100 percent to 75 percent, and their share of private sector deposits decreased even further to 64 percent. Public banks' share of foreign exchange deposits decreased from 92 percent in 2004 to just 25 percent in 2007 -- primarily due to the 311 action against CBS.

¶6. (C) Despite their loss in market share, public banks maintain a dominant position with an estimated USD 28 billion in assets (80 percent of total assets), USD 15 billion in deposits (75 percent of total deposits) and USD 12 billion in credits (89 percent of total credits). CBS alone has the greatest market penetration across Syria, with over 100 branches and some 170 ATMs. CBS also benefits from a virtual monopoly on government business, as all institutions and public companies almost exclusively bank with CBS.

Despite Sanctions and Reputation for Corruption

¶7. (C) Contacts say CBS's dominance is primarily attributable

to its brand recognition and market penetration after a 40-year industry monopoly, despite its reputation for abysmal customer service and corruption. In one recent anecdote, a CBS loan officer in Aleppo demanded a USD 5,000 bribe from a local textile producer to approve a USD 75,000 loan to complete the financing for an Italian-made weaving machine on which the textile factory owner had already paid a USD 25,000 deposit. When the machine arrived from Italy some six months later, the factory owner went to collect the loan and learned that his loan officer had been fired. After explaining his situation, the new loan officer refused to honor his predecessor's commitment unless the customer paid him a USD 10,000 bribe. Unable to afford the second bribe, the factory owner raised the needed capital by selling his warehouse -- where the machine was to be installed -- and borrowing from his competitors. He now rents time on the weaving machine to repay his competitors.

¶8. (S/NF) According to Raed Karawani (strictly protect), whose law firm was hired in 2007 to conduct a feasibility study for restructuring Syria's public banks, the Industrial

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Bank is the most corrupt public bank in the country. Karawani said that Industrial Bank's officers over the last 20 years were reknowned for approving any size loan for a 10 percent bribe. In his audit of the bank's books, Karawani saw numerous bad loans on the bank's ledger that -- instead of being written off -- had been repeatedly rescheduled over the last 10 to 15 years until the interest on them now far exceeds the principal.

¶9. (C) Although Treasury's 311 action cut CBS off from the U.S. financial system, contacts report that CBS is able to offer letters of credit (L/C) in Euros. To finance trade with external partners in U.S. dollars, CBS reportedly issues the L/C in Euros and offers same-day settlement to avoid penalizing customers for exchange rate fluctuations.

Real Estate Bank - A Regime Cash Cow

¶10. (S/NF) Karawani and Dr. Shadi Karam (strictly protect) separately told us that the only profitable Syrian public bank is Real Estate Bank (REB), which reportedly earns over USD 110 million annually -- largely from its monopoly on processing credit card and ATM transactions. A Lebanese-French citizen who recently became CEO of Syria's second largest private equity company, Karam said the SARG had hired him in 1996 to bring a credit card transaction processing capability to Syria. According to Karam, he chose to establish the credit card business inside REB instead of CBS because then-President Hafez al-Asad's brother-in-law and economic advisor, Muhammad Makhoulf (father of Specially Designated Nationals Rami and Hafiz Makhoulf), had been on the REB board of directors. Realizing his task would require cutting through reams of SARG red tape, Karam said he correctly assumed he would need someone of Muhammad Makhoulf's influence as a partner. Karam negotiated an arrangement between REB and FransaBank of Beirut -- reportedly still in use today -- whereby REB operates all credit card point-of-sale units around the country but FransaBank actually facilitates the external transactions with Visa and MasterCard.

¶11. (S/NF) Karawani added that REB also has a "near monopoly" on public banking ATM transactions. In addition to REB's own estimated 140 ATMs, REB reportedly operates and processes transactions for CBS's 170 ATMs. As debit cards become increasingly popular in Syrian society, Karawani says REB is positioned to collect even more ATM fees and continue to "make money out of air."

REB Wants Out from Under 311 Action

¶12. (C/NF) In early March 2009, a Dutch consultant to REB asked Post how U.S. sanctions might affect REB's plans to open an account in a U.S. bank in order to "execute U.S. dollar transactions." In response to our inquiry about CBS's relationship with REB, REB Treasurer and Foreign Relations Manager Kamel Adla provided copies of a request from REB to the Minister of Finance dated July 23, 2008, for permission to "terminate CBS's contribution of SYP 3 million (USD 63,025), or 0.2 percent, of REB's SYP 1.2 billion (USD 25.2 million) capital." Adla also provided a copy of the SARG's

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response -- Prime Minister Muhammad Naji Utri's Decision No. 5533 of December 15, 2008 -- which transferred CBS's shares in REB to the Syrian Public Establishment for Insurance. (Note: We do not know if REB was successful in finding a U.S. correspondent bank after ridding itself of CBS ownership. End note.)

¶13. (S/NF) American Express representative Kamal Abu Shaar (strictly protect) told us that Rami Makhoulf is employing a similar strategy to try to free his OFAC-blocked chain of duty free stores, RAMAK. Makhoulf's attorneys are reportedly filing a legal petition with OFAC arguing that RAMAK should be "un-blocked" because Makhoulf recently sold his shares in the company. Shaar said that about USD 100,000 in pending AmEx transactions with RAMAK had been frozen after the duty free chain's 2008 Treasury designation, which Makhoulf hoped to recoup by removing himself from RAMAK's ownership.

Politics Thwart Attempt to Restructure Public Banks

¶14. (S/NF) Karawani said Deputy Prime Minister for Economic Affairs Abdallah Dardari had been frustrated by Ba'ath Party political resistance to external recommendations to (a) close Industrial Bank, (b) merge the minimally active Agricultural Cooperative Bank into CBS, (c) make all public banks offer the same general services rather than specialization, and (d) lay off hundreds of bank employees. CBS, whose payroll is said to number around 5000, is, however, reportedly considering a proposal to "absorb" 1000 of its existing employees by implementing a two-shift workday, from 0800-1400 and 1400-2000.

In Need of a Technical Partner

¶15. (C/NF) General Manager of Bank Audi Syria Bassel Hamwi (strictly protect) remarked that CBS's performance is difficult to assess because -- unlike Syria's private banks -- no independent analysis of CBS is publicly available. He described Syria's entire public financial sector -- the Central Bank, Ministry of Finance, and the aforementioned public banks -- as in desperate need of a "technical partner" to build the necessary capacity for operating in the modern era. Hamwi explained that different public banking entities had, at times, worked with various European technical consultants funded by the World Bank, EU, and development agencies, but the lack of a government-wide strategy and a consistent partner limited the programs' effectiveness. He surmised that Syria would always be too suspicious of U.S. intentions to accept American assistance, if any were ever offered.

Bilateral Trade Banks

¶16. (S/NF) While market trend lines gradually shift towards private banking, some regime stakeholders are driving the expansion of public banks -- ostensibly to facilitate Syria's

expanding trade relationships with Iran, Turkey and Iraq. The most oft-reported example of this effort is the Syrian-Iranian Commercial Bank (SICB). As reported in refs B

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and E, SICB is a joint venture primarily between Bank Saderat of Iran and the Commercial Bank of Syria, with additional capital to be provided by the Saderat subsidiary Ghadir Investment Company, Syrian businessman Khalil Sultan al-Abed, and yet to-be-determined public shareholders. Over the past two years, Syrian trade delegations to Baghdad and Ankara have publicly announced SARG support for a Syrian-Iraqi Commercial Bank and a Syrian-Turkish Commercial Bank as evidence of Syria's deepening economic relationships with both countries, although Post is unaware of any significant progress towards opening either bank. (Comment: We doubt that either Turkish or Iraqi banks are eager to partner with CBS. End comment.)

Comment

¶17. (C) Syria's dingy concrete public bank buildings, with long customer lines and unmotivated employees, stand in sharp contrast to the turquoise, purple, red and glass private bank branches that now dot the brown Damascus cityscape. To a society hungry for technology and education, the public banks seem like vestiges of a waning era that are unable to evolve in this increasingly competitive sector of the economy. As the famously thrifty Syrians become more sophisticated banking consumers, the public banks will rely even more on government patronage and transaction monopolies to survive.
CONNELLY